

## **Treasury Report to Congress: Small Business Lending Program a Success** (February 2012)

The U.S. Treasury Department sent a report to Congress last month showing that the Small Business Lending Fund (SBLF), the program set up to boost lending to small businesses, is projected to earn an unexpected profit of \$80 million, a significant increase from the initial \$1.3 billion the program was expected to cost.

The projected profit is due to several factors, including a reduction in projected default rates for participating institutions, fewer actual investments than initially forecast and a decrease in Treasury's cost of raising funds, the Treasury said.

"This effective program is helping small businesses grow, create jobs and support families in communities across the nation while providing value to all Americans," wrote Don Graves, Treasury's deputy assistant secretary for small business, community development and housing policy, on the Treasury website.

In the report, the Treasury found that financial institutions participating in the SBLF have increased lending to small businesses by \$3.5 billion, or 10 percent, over baseline levels. And more than 60 percent of the institutions participating in the program have increased lending by at least 10 percent, the threshold banks must maintain to pay the lowest dividend on the borrowed funds.

The SBLF was created by Congress in September 2010 as part of the Small Business Jobs Act. The Treasury was heavily criticized by Congress for taking nine months to get the program off the ground, and later by CSBS and state banking regulators over concern regarding the approval process and conservative risk tolerance. The SBLF approved fewer than half of the 932 banks that applied for the program, an amount less than 15 percent of the \$30 billion fund.

### **Q&A with Louisiana Commissioner, CSBS Chairman John P. Ducrest on the Small Business Lending Fund**

CSBS staff interviewed John P. Ducrest, Louisiana Commissioner and Chairman of CSBS, to get the perspective of a regulator on the Treasury's announcement.

Examiner: In a recent report to Congress, the U.S. Treasury Department stated that the Small Business Lending Fund is working and is a success. The agency reported a projected profit of \$80 million and said that as a result of the program, lending to small businesses is up by \$3.5 billion, or 10 percent, over baseline levels. Based on data provided in the report, do you share this same view regarding the program?

Ducrest: I don't doubt the program is making money, and I support their recognition of the need to exercise prudence with taxpayer money. What is troubling is that Treasury is not being held accountable from a scale perspective. So little of the fund was used, and those additional potential investments could have had a much broader economic impact.

Examiner: There are more than 7,000 community banks small enough to have potentially qualified for the SBLF, but only 933 applied. And a mere 332 financial institutions were approved. Why do you think so few institutions applied for the program and what does it say that less than half were approved?

Ducrest: I think the number of institutions that applied was low because government officials were too limiting in which banks qualified for the program. Treasury denied a substantial number of institutions. Throughout the approval process, we were told they did not have any room for taking risk in these investments, and therefore, they only invested in institutions with little trace of regulatory uncertainty. Clearly they over-compensated, even by their own standards. They expected much higher default rates with a cost of \$1.3 billion. Now, they're looking at a huge swing in the other direction. This tells me they did not come close to using all the investment leeway their own projections provided. Now, many perfectly healthy banks, which were ready to lend to small businesses, missed out on a great opportunity. This undoubtedly had an impact on local economies and jobs.

Examiner: CSBS and many individual state banking regulators, including you, submitted letters to the Treasury expressing concern regarding aspects of the SBLF approvals process that led to less than half of banking institutions that applied for the program being approved. What do you believe the Treasury could have done differently to make more of an impact in small business lending?

Ducrest: I believe they could have been more transparent during the approval process. Institutions tried to work with Treasury throughout the application process and were not able to resolve their issues. Many of these institutions received endorsements from state and federal regulators to participate in the program. And from my perspective, in many cases the issues Treasury was hung up on were not insurmountable by any means. As I mentioned earlier, it seems Treasury's ultra-conservative approach to this program precluded many qualified institutions from participating. Roughly \$18 billion of the fund was not applied for. That was out of Treasury's hands. However, more than half of the institutions that applied for funding were denied, and I don't believe all those denials were warranted. This was a lost opportunity to stimulate small business on a larger scale.

Examiner: The Senate Small Business Committee held a hearing in October regarding the Treasury's SBLF program. During the hearing Louisiana Senator and Committee Chairman Mary Landrieu indicated that she may develop an SBLF 2.0, a new version of the program, after receiving input from participating banks, small businesses and agency officials. Would you support an SBLF 2.0? If so, what recommendations would you give to guide the Treasury the second go-round?

Ducrest: Clearly there are some lessons learned from the SBLF, which could be applied to an SBLF 2.0. With all due respect to the Treasury Department, I do not think they are best suited to administer the program. Instead, there needs to be consensus on the best manager of the program. Ultimately, the biggest challenge of an SBLF 2.0 will be to properly calibrate the risk of the program and to avoid being too risk-adverse. The effort of implementing such a program is definitely worth it, since the program is fundamentally about economic development and jobs. I look forward to working with Senator Landrieu on this project to identify possible solutions and finding ways to improve the SBLF.